PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Telecommunications Division **RESOLUTION T-16711**
Carrier Branch **January 16, 2003**

R E S O L U T I O N

RESOLUTION T-16711. THE SIERRA TELEPHONE COMPANY, INC. (U-1016-C). GENERAL RATE CASE FILING IN COMPLIANCE WITH G. O. 96-A, PARAGRAPH VI, AND DECISION NUMBERS 01-02-018 AND 01-05-031.

BY ADVICE LETTER NO. 285 FILED DECEMBER 21, 2001.

Summary

This resolution addresses the General Rate Case filed by Sierra Telephone Company, Inc. (Sierra) through Advice Letter 285 in compliance with D.01-05-031. Sierra proposes a) no changes to its rates or charges, b) an intrastate ROR of 10.00%, the same rate of return granted in its previous GRC filing in 1997, and c) an increase of $759,789 in its California High Cost Fund-A (CHCF-A) draw for year 2003.

This resolution authorizes total intrastate revenue in the amount of $23,644,229 for Sierra for the test year 2003. This represents a reduction of $2,902,149 to Sierra's estimate of $26,546,378 for total intrastate revenue for 2003. The Total Intrastate Rate Base amount for Sierra is $37,443,117 with an overall Intrastate Rate of Return of 10.00% for the test year 2003. Also authorized by this resolution is CHCF-A support for Sierra for test year 2003 of $11,649,067. This amount represents a reduction of $2,101,077 or 15.28% decrease from the CHCF-A 2002 support of $13,750,144. This reduction is due to adjustments made to revenues, expenses and rate base.

Appendix A compares the Telecommunications Division's (TD's) and Sierra's Test Year 2003 Total Company Results of Operations before any CHCF-A adjustment. Appendix B compares TD's and Sierra's Interstate and Intrastate Results of Operations before any CHCF-A adjustment. Appendix C compares TD's and Sierra's Intrastate Results of Operations estimates after Sierra's proposed CHCF-A increase and after TD's proposed adjustments. Appendix D shows TD's calculation of the Net-to-Gross Multiplier and the change in the gross intrastate revenue requirement based on an adopted intrastate rate of return of 10.00%.

Background

The Sierra Telephone Company, Inc. (Sierra), a local exchange telephone utility based in Oakhurst, California, provides local exchange telephone service in parts of Mariposa and Madera counties. Sierra serves approximately 23,000 access lines in its three telephone exchanges: Coarsegold, Raymond and Mariposa.

In Decision (D.) 01-05-031, the California Public Utilities Commission (CPUC) set in motion the waterfall[1] provision in 2002 for six small LECs if they do not each file a General Rate Case (GRC) by the end of 2001.[2] Sierra filed Advice Letter (AL) No. 285 on December 24, 2001, with a Test Year of 2003. The last GRC filed by Sierra was in 1995 through Application 95-12-077 and its latest intrastate results of operations were authorized by Decision 97-04-032 dated April 9, 1997.[3]

In AL 285, Sierra proposes a) no changes to its rates or charges, b) an intrastate ROR of 10.00%, the same rate of return granted in its previous GRC filing in 1997, and c) to increase its CHCF-A draw by 5.44% or an additional $759,789 for year 2003.

Notice/Protests

Sierra states that a copy of the Advice Letter was mailed to competing and adjacent utilities and/or other utilities. Notice of AL 285 was published in the Commission Daily Calendar of December 24, 2001. Notice of the AL filing was made to customers by bill insert on December 21, 2001. No protest to this AL filing has been received.

TD held a Public Meeting in Oakhurst on August 12, 2002, at which time Sierra was given an opportunity to explain its filing to its customers. Sierra's customers were also given the chance to ask questions of Sierra and the TD staff, and to comment on Sierra's rates and services. Sierra's customers were given notice of the Public Meeting through bill inserts. The notice of Public Meeting was also published in the August 2, 2002 issue of the CPUC Daily Calendar. No customers attended the Public Meeting.

[1] The waterfall provision refers to the 6-year phase down of the CHCF-A funding level beginning in 1998, the year after the completion of a GRC. The funding levels are 100% of the for the first 3 years, i.e., 1998, 1999 and 2000; 80 % the fourth year, i.e., 2001, 50% the fifth year, i.e., 2002; and 0% thereafter.
[2] The six companies are Evans Telephone Company, Happy Valley Telephone Company, The Ponderosa Telephone Company, Sierra Telephone Company, Inc., The Siskiyou Telephone Company, and The Volcano Telephone Company.
[3] In Application 95-12-077, Sierra requested to earn a 15% rate of return on equity (ROE) while reducing rates by $500,000; granted as modified by Decision 97-04-032, with a 10.94% authorized ROE and a reduction in rates of $1.1 million. The mandated rates decrease were allowed to go into effect partly through elimination of the carrier's 8.57% billing surcharge and partly through elimination of charges for unlisted or unpublished number service. Basic residential monthly charges were maintained at their existing levels.

Discussion

Results of Operations

TD calculates that Sierra will earn in test year 2003 a total company overall rate of return of 14.18% at present rates as compared to Sierra's calculation of 10.16%. Since TD concludes Sierra is earning well above TD's goal of an overall rate of return of 10.00%, TD has proposed changes in Sierra's revenues, expenses, and rate base as discussed below. Appendix A compares Sierra's total company results of operations for test year 2003, as estimated by TD and Sierra.

Total Operating Revenues

Sierra's estimate of total company operating revenues at $42,455,031 exceeds TD's estimate of $40,260,065 by $2,194,966 or 5.5%. Differences between TD's and Sierra's estimates are described below.

Sierra's estimate of total company revenue for Local Network Services at $7,132,175 is $137,947 lower than TD's estimate at $7,220,122. In determining the test year total company revenues for Local Network Services, Sierra first developed access line growth rates using regression analysis. Sierra regressed historical access lines against time for the 1996-2001 period. In support of its regression analysis, Sierra submitted a coefficient of determination of 99%. The coefficient of determination measures the strength of the relationship between the actual historical access lines and time. A coefficient of determination closer to one (100%) indicates a greater degree of relationship; while a coefficient of determination closer to zero indicates a lesser degree of relationship. Based on the regression analysis, Sierra derived full year growth rates for access lines of 3.52% for 2002 and 3.39% for 2003. TD accepts Sierra's estimates of full year growth rate for access lines.

Instead of using the full year growth rate, Sierra applied mid-year growth rates to the Average Quantity in Equivalent Units (AQEU) to develop local revenues through 2003. The AQEU is derived from the total billed amount for each service in year-end 2001 divided by the tariffed amount. The mid-year growth rate is one-half of the full year growth rate. TD determined that if mid-year growth rates were used, they would underestimate the local revenues for the full 2003 test year.

TD's methodology for estimating local revenues is similar to Sierra's but provides a more realistic projection of the expected revenues for 2002 and 2003. TD escalated the AQEU year-end amount for 2001 by the full year growth rates, and then multiplied by the tariff rates to determine the local revenues for 2002 and 2003. Since the AQEU are year-end amounts, by applying the full year growth rate, instead of the mid-year growth rate, results in a more accurate estimate for 2002 and the 2003 test year.

Sierra and TD also differ on estimates for Billing and Collection revenues. Sierra projected a two percent growth rate in both the intrastate and interstate Billing and Collection revenues from its subsidiary Sierra Tel Long Distance (Sierra Tel). TD rejects the two percent proposed growth rate because it is low compared to historical average growth rates. For the 1999-2001 period, the three-year average growth rates for intrastate and interstate Billing and Collection are 35.65% and 31%, respectively.[4] TD uses these three-year historical average rates to project Sierra's 2003 Billing and Collection intrastate and interstate revenues. TD's recommended intrastate and interstate Billing & Collection revenues are $194,553 and $43,978, respectively. TD's Billing & Collection revenues and other data updates[5] result in an updated Miscellaneous revenues of $1,617,858.

Revenues in the 2003 Interstate Network Access Services also changed from $11,495,520 to $11,563,085. This was due to Sierra's updating its data to reflect projections based on using 2001 actual year-end numbers, instead of using nine months data to project 2001 numbers in its original GRC filing.

Revenues in the 2003 Long Distance Network also changed from $18,049 to zero in Sierra's updated 2003 results of operations. Sierra stated that the $18,049 was in fact intrastate Private Line revenues and should have been recorded under Network Access Services-Intrastate. Therefore, Sierra deleted the $18,049 from the Long Distance Network revenues and recorded the amount under the Network Access Service-Intrastate revenues. TD finds Sierra's correcting of the misidentified Network Access Service-Intrastate revenues to be reasonable.

Total Operating Expenses

Sierra's estimate of total company operating expenses at $33,508,209 is greater than TD's estimate of $28,616,995 by $4,891,214 or 17.1%. A comparison of TD's and Sierra's estimates of total operating expenses for test year 2003 is shown in Appendix A. Differences between TD's and Sierra's estimates are described below.

For operating expenses, Sierra used 1996-2001 actual cost study data and ran regression analysis on each account. Sierra then estimated the 2002 and 2003 expenses based on the regression analysis with the exception of Depreciation Expense, Billing & Collection Expenses, and Directory Expenses. TD accepts Sierra's alternative methodology for the three exceptions.

[4] These growth rates are already adjusted to reflect that Sierra would no longer receive Billing and Collection revenues from AT&T because their agreement had terminated as of December 31, 2001.
[5] Miscellaneous revenues were updated using a full year of 2001 data rather than the nine months of data in Sierra's original GRC filing.

TD, however, disagrees with Sierra's regression analysis. Fourteen out of twenty-five expense accounts regressions had coefficient of determination results that were too low (9.36% to 79.83%) for TD to accept.

For this reason TD used Sierra's recorded labor and non-labor expenses and applied the constant dollar method to estimate Sierra's 2003 expenses. The Commission in Siskiyou's 1997 test year rate case proceeding discussed and adopted Commission staff's use of the constant dollar methodology. In Finding of Fact 6 of Resolution T-16006, the Commission found "…TD's methodology in estimating expenses reasonable and adopt TD's recommended test year 1997 expenses contained in Appendix A." [6]

TD used Sierra's recorded expense figures from the annual reports for the years 1999, 2000 and 2001[7] and then applied the recorded inflation factors for labor and non-labor for each year to convert the recorded expenses to constant 2001 dollars. [8] TD then took the three-year constant dollar average and applied the estimated inflation factors for 2002 and 2003. TD's estimation of utilizing the constant dollar method resulted in $18,197,420 for operating expenses, 20.8% less than Sierra's estimates of $22,979,132.

To calculate depreciation expenses, both TD and Sierra utilized the same methodology and depreciation rates previously adopted by the Commission for Sierra. The difference in depreciation expense of $109,502 is due to the difference in plant-in-service. TD's depreciation expense was computed using TD's plant-in-service estimates for 2002 multiplied by the current depreciation rates to derive 2002 figures. To estimate 2003 figures, TD used its projected depreciable plant in service for 2002 and applied the current depreciation rates previously approved by the Commission for Sierra in Resolution T-14000.

Taxes

TD's estimate of Total Operating Taxes at $4,777,957 is 29.2% greater than that computed by Sierra. Although TD and Sierra both used a Corporate State Franchise Tax (CCFT) rate of 8.84% and a federal income tax rate of 34.00%, differences between

[6] At page 5 of Resolution T-16006, the Commission stated "Generally for traditional GRCs, the Commission adopts the constant dollar method".
[7] Revised ARMIS Report (FCC ARMIS 43-02 Report Format) of Sierra's Annual Reports for 1999, 2000 and 2001.
[8] TD used the March 2002 DRI-WEFA U.S. Economic Outlook estimates of Non-Labor and Wage Escalation Factors for 2002-2004. as follows:

Year	Labor	Non-labor
2000	1.022	1.036
2001	1.034	1.000
2002	1.028	0.999
2003	1.018	1.018
2004	1.026	1.021

Sierra's and TD's estimates of income, revenue, and expenses resulted in the Total Operating Taxes differences.

Rate Base

TD examined Sierra's Rate Base components, which include Telephone Plant-in-Service, Telephone Plant-under-Construction, Materials & Supplies, Customer Deposits, and Working Cash. TD concurs with Sierra's estimate of Materials & Supplies and Customer Deposits as updated. TD disagrees with Sierra's estimates of Plant-in-Service, Plant-under-Construction, and Working Cash.

TD's Working Cash test year 2003 estimate is $1,314,508, or 14.3% lower than that computed by Sierra, due to TD's higher revenue and lower expense estimates.

TD's review of Sierra's plant-in-service showed that Sierra had a large increase in both land and building purchases in 2001. TD visited the building during the field inspection and discovered that it remains vacant, except for a portion that was leased to a game development company from whom Sierra had bought the building. Sierra indicated that it acquired the building in 2001 for $912,874, and paid $391,000 for the land as part of the total valuation. Since the purchase was made in 2001, Sierra included the building and land in the regulated rate base for years 2001, 2002, and 2003. Sierra notes that the first floor office space is currently leased to the game company rent-free as part of the purchase agreement until August 1, 2003. Sierra is still uncertain as to which personnel will be occupying the second floor space. Since the building and land is not currently used and useful, TD does not believe Sierra should be allowed to include the purchase of the building and land in the rate base for the 2003 test year. Therefore, TD recommends an average plant-in-service of $125,670,271, which excludes $1,303,874, the total cost of the building and land.[9]

Sierra's Plant-under-Construction amounts for years 2002 and 2003 were based on a historical review of the account rather than specific work orders anticipated to be opened at year-end. It is TD's policy to disallow any Plant-under-Construction in rate base because the utility, not ratepayers, should bear the full burden of project construction costs until the project is operative. Additionally, Sierra's estimates are questionable because the Plant-under-Construction estimates were based on projections of historical accounts instead of actual work orders. Consistent with TD's policy on Plant-under-Construction and insufficient support for Sierra's estimates, TD recommends that the total Plant-under-Construction of $2,100,000 be excluded from Sierra's rate base estimates.

Separations

[9] Average plant in service also was updated for a full year of 2001 data rather than the nine months of data in Sierra's Original GRC filing.

Sierra provides both intrastate and interstate telecommunications services, subject to the regulation of the CPUC and FCC, respectively. Because Sierra's property serves both jurisdictions, the utility's revenues, expenses, taxes, investments, and reserves are allocated (separated) between interstate and intrastate services according to FCC rules. TD has reviewed Sierra's separation factors and finds them to be reasonable. Appendix B compares Sierra's and TD staff's total company interstate and intrastate results of operations for test year 2003 using these separation factors.

Cost of Capital

Sierra requests an overall intrastate rate of return of 10.00%. This is the same rate of return that was authorized under D.97-04-032 for its last general rate case filing for test year 1997.

The Return on Equity for all rural ILECs should be the same since the systematic and non-diversifiable risks faced by all rural ILECs are similar. As a matter of practice, Decision D.97-04-036 in A.95-12-073[10] adopted an 'overall' rate of return of 10.00% for all rural ILECs. Based on information provided, TD recommends that the Commission should approve Sierra's request for an overall rate of return of 10.00% at this time. This approval should not set a precedent for any future or pending small ILEC GRC proceeding.

Net-to-Gross Multiplier

The net-to-gross multiplier indicates the unit change in gross revenues required to produce a unit change in revenues. Appendix D shows TD's computation of Sierra's net-to-gross multiplier. The net-to-gross multiplier of 1.66207 means that a change of $1,662 in gross revenue would be required to produce a change of $1,000 in net revenue. For Sierra, based on a recommended state rate base of $35,601,445 and rate of return of 10.00%, the recommended intrastate revenue requirement change required is a reduction of $1,071,535.

CHCF-A Support

D.01-02-018 approved Settlement Transition Agreements (STAs) between Pacific Bell and the small Local Exchange Companies (small LECs). Monies that Pacific Bell paid the small LECs through toll and access pool settlements were replaced by authorized draws from the CHCF-A. The CHCF-A itself was originally established by D.85-06-115 as a means of subsidizing reasonable basic exchange rates for the customers of small LECs that adopted Pacific's statewide average toll, tool private line, and access rates (settlement pools). D.01-02-018 required the small LECs' replacement funding for the STAs be subject to the same rules that apply to current draws from the CHCF-A,

[10] In D.97-04-036 the Commission authorized California-Oregon Telephone Company a 10.00% return on rate base for its 1997 test year as requested in A.95-12-073 (California-Oregon's 1997 General Rate Case application).

namely rates shall be increased to a ceiling as necessary and both the means test and the waterfall provisions should apply.

In 2002, Sierra's draw from the CHCF-A was $13,955,628 of which $205,484 represents nonrecurring costs, specifically its 2001 IntraLATA Presubscription Expenses and change in its weighting of Digital Equipment Minutes (DEM). [11] DEM are the minutes of holding time of originating and terminating local dial equipment and serves as a standard cost allocator. For small local exchange carriers, the DEM is weighted or multiplied to allocate additional costs to the interstate jurisdiction. Since $205,484 is a nonrecurring cost that occurred in 2001, TD removed this amount from the 2002 CHCF-A draw. The adjusted 2002 CHCF-A draw is $13,750,144.

Sierra's request for an additional draw from the CHCF-A of $759,789 included a three-year amortization recovery of rate case expenses in the total amount of $11,941. From Sierra's workpapers, TD finds that an additional draw of $747,681 would have been sufficient for the company to earn a 10.00% intrastate rate of return prior to any TD adjustments. Including the recovery expense after adjustments would cause Sierra's intrastate rate of return to exceed 10.00%.

TD calculated Sierra's CHCF-A support for test year 2003 at present rates to be $10,898,442. The CHCF-A 2003 support is derived from using Sierra's 2002 initial draw of $13,955,628, adding the $2,951,674 NECA estimated USF Federal support for 2002, subtracting Sierra's projected 2003 USF Federal support of $5,803,376[12], and removing the non-recurring DEM cost of $205,484. [13]

However, if Sierra is authorized to receive $10,898,442 in CHCF-A support, then based on TD's adjustments in revenues, expenses and rate base, Sierra's intrastate rate of return would be at 10.57%, which would exceed the 10.00% goal. Therefore, for test year 2003, TD 's computation of Sierra's adopted CHCF-A requirement is $9,826,908 based on its recommended revenues, expenses, rate base and overall intrastate rate of return of 10.00%.

Comments

The draft resolution of the Telecommunications Division on this matter was mailed to the parties in accordance with PU Code Section 311 (g)(1).

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[11] Resolution T-16619, page 8 and Page 13 of the Appendix.

[12] Federal USF support is based on the 2003 projected payments for the California Exchange carriers as filed by the National Exchange Carriers Association, Inc. (NECA) on October 1, 2002 with the Federal Communications Commission.

[13] This calculation follows CHCF-A Implementation Rules in accordance with guidelines summarized in the Appendix of D.91-09-042.

On January 2, 2002 Cooper, White & Cooper, LLC (Cooper) filed timely comments on behalf of Sierra. Cooper raises the following issues in the draft resolution:

1. TD's understatement of the test year expenses due to the use of constant dollar method.

2. TD's disallowance of investment associated with a building placed into operation in late 2002.

3. TD's exclusion of CWIP in the rate base.

4. TD's exclusion of expenses associated with E911 and Inside Wire maintenance.

On the use of the constant dollar methodology (CDM) in estimating expenses, Sierra argues the draft resolution's 2003 test year expenses (not including depreciation) are less than Sierra's actual recorded expenses for 2001. Sierra asserts that it is completely implausible to assume that a company experiencing increasing costs over the last several years will realize lower expenses than it incurred two years previous. Sierra also states that based on 1996 through 1999 actual expenses, the CDM as applied in the draft resolution consistently underestimated expenses for years 1999, 2000 and 2001.

Sierra noted that the Commission had rejected the use of the CDM when the forecast of test year expenses was below the expenses incurred in the last recorded year. In a water rate case, the Commission staff forecasted 1987 test year expenses for office supplies that were lower than the 1985 recorded costs. In that case, the Commission relied on the trending methodology used by the utility instead of the CDM[14].

Furthermore, Sierra lists significant increases in expense accounts that have been growing faster than the normal inflation rate used by the CDM, such as workers compensation, medical and pension costs, as well as life and general liability insurance costs. In addition, Sierra states that it has hired 29 new employees in the last two years to meet the demands placed on Sierra for regulatory compliance, customer service, maintenance and engineering.

While continuing to support its original expense estimates, Sierra proposes an alternative methodology that would take into account the abnormal expense increases previously described. Sierra's alternative methodology escalates actual 2001 expenses to 2003 using the CDM's growth factors, yielding $20,597,163. This amount is added to $942,000 of "known and measurable "expenses for 2002 and 2003 resulting in total

[14] California Water Service Company, 24 C.P.U.C.2d 68, 80-81.

company expenses of $22,482,575, which is $496,557 or 2.2% less than Sierra's original proposal of $22,979,132.

With regard to the disallowance of the investment (a building and land purchased) in rate base, Sierra claims that its personnel moved into the building in October 2002 and will occupy the warehouse in the summer of 2003. Accordingly, both the building and the warehouse will be used and useful during the 2003 test year, although a portion of those facilities will be used by an unregulated affiliate. Based on current plans, Sierra projects that approximately 60% of the facilities will be used for regulated telephone operations. On that basis, Sierra proposes including 60% of the investment in land and buildings in Sierra's 2003 test year rate base.

With regard to the exclusion of CWIP, Sierra points out that CWIP has consistently been included in the rate base in previous rate cases involving the small LECs in the computation of the rate base. Specifically, the Commission, in Sierra's 1997 rate case (D.97-04-034) approved the inclusion of CWIP. Likewise, the Commission also consistently permitted the inclusion of CWIP in Sierra's annual CHCF-A means test filings. Sierra also notes that Commission resolutions adopted on December 17, 2002 addressing the Volcano and Siskiyou rate cases reinstated CWIP after the draft resolution proposed disallowing it. Thus, the exclusion of CWIP is in direct contradiction of the Commission's policies and procedures on the preparation and filing of general rate cases. Sierra's reliance on the recovery of the CWIP in the rate base has influenced Sierra's investment plans.

With regard to the exclusion of expenses associated with E911 and Inside Wire maintenance, Sierra states that in its original rate case filing, it did not include expenses associated with E911 and Inside Wire maintenance. However, Sierra's updated workpapers provided to TD in a data request did reflect these total company costs for years 1999-2001. Therefore, Sierra requests that the historical expenses data for 1999-2001 must be updated to include E911 and Inside Wire maintenance expenses.

TD's Responses to Comments

Although Sierra notes that the draft resolution's 2003 test year expenses are less than its actual, recorded expenses for 2001, this observation does not justify Sierra's 2001 expenses, nor is it sufficient grounds to discard the CDM for all expenses. Because the 2001 recorded cost have not been adjusted for ratemaking purposes, and the company should have incentives to control costs, the 2001 actual expenses should not be the primary factor in forecasting test year expenses as proposed by Sierra in its alternative methodology.

TD had originally utilized the CDM to forecast all of Sierra's 2003 test year expenses because it is a Commission approved and accepted methodology. However, pursuant to comments and further review, TD finds that using the CDM may not be the most appropriate method to forecast all expenses for a particular company.

The method that should be used to forecast a specific expense will, at least in part, depend on the characteristics of the specific expense. If an expense account shows a clear historical trend, time-series regression analysis may be a better tool to capture that trend in the test year, provided that the trend is expected to continue in the future. For regression analysis to be acceptable, it must also meet certain statistical standards, such as a high coefficient of determination close to one (100%). On the other hand, if an expense account fluctuates over time, or if the regression yields a low coefficient of determination, then time-series regression analysis typically does not yield sound statistical results. Under circumstances when there has been a fluctuation in expenses in the years leading up to the test year, the CDM is more appropriate for determining test year expenses, as Sierra acknowledges in its comments at page 2.

Therefore, TD recommends that the time-series regression analysis be used as an alternative method to forecast 2003 test year expenses when appropriate. TD examined the trend for various accounts and utilizing Sierra's 1996-2001 actual recorded expenses, ran a regression analysis on the totals of each of the four major expense accounts: Plant Specific, Plant Non-Specific, Customer Operations and Corporate Operations. Based on the regression results, TD recommends that regression analysis be used to estimate 2003 expenses for Customer and Corporate Operations only, because these two major accounts had coefficient of determination results in excess of 90%. For the Plant Specific and Plant Non-Specific accounts, TD continues to recommend using the CDM to forecast the 2003 test year expenses because these accounts had low coefficient of determination results. Based on a combination of regression analysis and CDM, TD now recommends a 2003 test year total expense of $20,154,610, which is $1,957,190 or 10.8% higher than its original proposal of $18,197,420. TD's revised recommendation is $2,327,965 or 10.4% less than Sierra's alternative methodology of $22,482,575[15]. Additionally, it should be noted that TD's revised methodology results in a 10.8% increase from TD's original position, whereas Sierra's alternative methodology only represents a 2.2% decrease from Sierra's original recommendations.

On the issue of the exclusion of CWIP, TD acknowledges that the Commission has historically allowed the inclusion of short term CWIP in the rate base in general rate cases and in the annual CHCF-A filings. TD recognizes the adverse effect that the exclusion of short term CWIP could have on Sierra's finances and as well as the benefit that customers could derive from paying for the construction costs as they occur rather than paying for the additional financing costs for the life of the assets through AFUDC

[15] Although TD's overall recommendations for the four major accounts is less than Sierra's, it should be noted that TD's forecast of Corporate Operations is even slightly higher than Sierra's due to the small difference in the underlying data.

and incurring additional depreciation expense. Therefore, TD now recommends that short term CWIP be allowed for ratemaking purposes for Sierra's 2003 test year.

TD reviewed Sierra's submission of additional data that was provided to support its comments. The utility's CWIP figures are now separated between short term, long term and total. Based on the average of the percentage of short term CWIP to total CWIP for the three most recent years, TD derived a short term CWIP percentage of 75%. TD then applied the 75% to Sierra's projected total CWIP for years 2002 and 2003 to derive the short term CWIP for the test year. TD, therefore, recommends a short term CWIP of $1,575,000 (75% of $2,100,000) in the 2003 test year rate base estimate, which is 25% less than Sierra's estimate.

On the issue of the disallowance of the investment (purchase of building and land), Sierra was originally uncertain about the time line and as to which personnel will occupy the building. TD initially determined that the investment was not currently used and useful and therefore disallowed the entire value of the investment. However, pursuant to comments, Sierra was then able to submit a schedule that summarizes the time line under which portions of the building have become or will become used and useful in 2003 for regulated telephone operations. Based on the current plans, Sierra projected that approximately 60% of the facilities will be used for regulated telephone operations by 2003.

Sierra had also noted that a similar issue existed in Siskiyou's 1997 general rate case and that the Commission had permitted the questioned building to be placed in the rate base. To alleviate concerns, the Commission required the company to provide a letter to the Director of TD notifying the Commission of occupancy dates for the new building.

TD reviewed Sierra's submission and determined that allowing $782,324 (60% of the total investment in land and building) in plant-in-service in Sierra's 2003 test year rate base is reasonable. Since the schedule details the time line of occupancy, TD is able to determine that 60% of the investment will be used and useful for regulated telephone operations in 2003. However, TD reserves the right to make the necessary adjustments in the plant-in-service and to its revenue if the building (both office space and warehouse) does not achieve the 60% occupancy by year end 2003. Accordingly, Sierra should notify the Director of TD by letter of the occupancy dates of the building. If considerable delays are faced by Sierra, which prevents the 60% occupancy by year end 2003, it should file an advice letter detailing the reasons of the delay. Furthermore, Sierra shall indicate how the change in rate base would affect its overall results of operations and propose adjustments to its revenue.

On the issue of the exclusion of expenses associated with E911 and Inside Wire maintenance, TD has reviewed and made the necessary corrections to Sierra's 2003 test year expense accounts.

In summary TD has a) utilized the regression method for Customer and Corporate Operations and maintained the use of the CDM for Plant Specific and Non-Specific to forecast 2003 test year expenses, b) increased the 2003 test year Customer and Corporate Operations intrastate expenses to $9,077,202, c) included short term CWIP of $1,575,000 in the 2003 test year rate base estimate, d) increased $782,324 (60% of total investment) in plant-in-service in the 2003 rate base estimate, and e) included E911 and Inside Wire expenses in the 2003 intrastate expense estimates of $59,646. These adjustments revise TD's intrastate operating expenses from $15,728,438 to $17,244,505, total intrastate rate base from $35,601,445 to $37,443,117, and CHCF-A support from $9,826,908 to $11,649,067.

Findings

1. Sierra filed its GRC on December 21, 2001, with a Test Year of 2003 in compliance with Decision 01-05-031.

2. Sierra requests the following for test year 2003:

   - An increase in its CHCF-A draw for 2003 by 5.44% or $759,789 for a 2003 CHCF-A support of $14,715,417;
   - An intrastate rate of return of 10.00%, the same return granted to them in their last GRC filing in 1997;
   - No change in its rate or charges; and
   - A total intrastate rate base amount of $38,051,210.

3. The Telecommunications Division (TD) recommends the following for Sierra for test year 2003:

   - A California High Cost Fund-A (CHCF-A) support of $11,649,067;
   - An Intrastate Rate of Return of 10.00%;
   - A revenue requirement increase of $750,626; and
   - A total intrastate rate base amount of $37,443,117.

4. The differences in the revenue, expenses, and rate base estimates between Sierra and TD result from both updates and the use of different methodologies.

5. The Commission finds TD's methodology in estimating revenues to be reasonable. The Commission therefore adopts TD's recommended intrastate revenues as shown in Appendix C.

6. The Commission accepts TD's recommended overall intrastate rate of return of 10.00% for Sierra.

7. The Commission finds Sierra's depreciation rates adopted in Resolution T-14000 for its 1997 GRC to be acceptable for ratemaking purposes for Sierra 's 2003 test year.

8. The Commission finds TD's recommended $11,649,067 CHCF-A support for Sierra for 2003 to be acceptable. The $11,649,067 CHCF-A support is based on the Commission's adoption of TD's Intrastate Results of Operations for Sierra for test year 2003.

9. The Commission finds TD's recommendation to include the total Plant-under-Construction of $1,575,000 to be reasonable.

10. The Commission finds TD's recommendation for Sierra to notify the Director of TD by letter of the occupancy dates of the building to be reasonable.

11. Commission approval is based on the specifics of this Advice Letter and does not establish a precedent for the contents of any future filings by small ILECs.

THEREFORE, IT IS ORDERED that:

1. The intrastate revenues, expenses, and rate base amounts for test year 2003 identified in Appendix C, column (E) are adopted for The Sierra Telephone Company, Inc.

2. The overall intrastate rate of return of 10.00% is adopted for Sierra.

3. Sierra shall notify the Director of TD by letter of the occupancy dates of the building. If considerable delays are faced by Sierra, which prevents the 60% occupancy by year end 2003, it should file an advice letter detailing the reasons of the delay and the effect of removing this building from its revenue. Sierra shall indicate how the change in rate base would affect its overall results of operations and propose adjustments to its revenue.

4. The depreciation rates submitted by The Sierra Telephone Company, Inc. in support of its General Rate Case Advice Letter No. 285 is adopted for ratemaking purposes.

5. The Sierra Telephone Company, Inc.'s CHCF-A draw for 2003 is $11,649,067.

This Resolution is effective today.

I hereby certify that this Resolution was adopted by the Public Utilities Commission at its regular meeting on January 16, 2003. The following Commissioners approved it:

/s/ WESLEY M. FRANKLIN

WESLEY M. FRANKLIN
Executive Director

MICHAEL R. PEEVEY
President
CARL W. WOOD
LORETTA M. LYNCH
GEOFFREY F. BROWN
Commissioners

I abstained.
/s/ SUSAN P. KENNEDY
Commissioner

APPENDIX A
THE SIERRA TELEPHONE COMPANY, INC.
TOTAL COMPANY RESULTS OF OPERATIONS
AT PRESENT RATES
TEST YEAR 2003

		SIERRA (a)	TD (b)	Utility Exceed Amount (c) = (a)-(b)	Percentage Change (d)
OPERATING REVENUES:					
1	Local Network Services	7,132,175	7,270,122	(137,947)	(1.90)
2	Local Services - CHCF-A	13,955,628	10,898,442	3,057,186	28.05
3	Long Distance Network	18,049	0	18,049	100.0
	Network Access Svces:				
4	Intrastate	3,196,334	3,118,523	77,811	2.50
5	Interstate	11,495,520	11,563,085	(67,565)	(0.6)
6	Interstate - USF	5,160,814	5,803,376	(642,562)	(11.1)
7	Miscellaneous	1,507,637	1,617,858	(110,221)	(6.8)
8	LESS: Uncollectible Rev.	(11,126)	(11,341)	215	(1.9)
9	**Total Oper. Revenues**	**42,455,031**	**40,260,065**	**2,194,966**	**5.5**
OPERATING EXPENSES:					
10	Plant Specific	9,039,700	6,168,340	2,871,360	46.5
11	Plant Non-Specific (less depr.)	2,315,200	2,250,170	65,030	2.9
12	Depreciation & Amortization	10,529,077	10,434,911	94,166	0.9
13	Customer Operations	4,379,932	4,328,300	51,632	1.2
14	Corporate Operations	7,244,300	7,407,800	(163,500)	(2.2)
15	Interstate Expense Adj. -USF	0	0	0	0.0
16	**Total Oper. Expenses**	**33,508,209**	**30,589,521**	**2,918,688**	**9.5**
OPERATING TAXES:					
17	Operating State Inc. Taxes	689,654	752,888	(63,234)	(8.4)
18	Operating Fed Income Taxes	2,353,715	2,575,424	(221,709)	(8.6)
19	Taxes Other Than Income	655,500	663,900	(8,400)	(1.3)
20	**Total Operating Taxes**	**3,698,869**	**3,992,212**	**(293,343)**	**(7.3)**
21	**Net Operating Revenue**	**5,247,953**	**5,678,332**	**(430,379)**	**(7.6)**
RATE BASE (Beginning + End of Year Average)					
22	Telephone Plant-in-Service	128,072,519	126,452,595	1,619,924	1.3
23	Tel. Plt Under Construction	2,100,000	1,575,000	525,000	33.3
24	Mat & Supplies	750,000	750,000	0	0.0%
25	Working Cash	1,533,208	1,426,908	106,300	7.4
26	Less: Deprec. Res.	(74,336,891)	(72,880,301)	(1,456,590)	2.0
27	Def. Taxes	(6,571,560)	(6,577,057)	5,497	(0.1)
28	Customer Deposit	(20,000)	(9,974)	(10,026)	100.5
29	RTB Stock	124,029	124,029	0	0.0
30	**Total Rate Base**	**51,651,305**	**50,861,200**	**790,105**	**1.6**
31	**Rate of Return**	**10.16%**	**11.16%**		

APPENDIX B
THE SIERRA TELEPHONE COMPANY, INC.
RESULTS OF OPERATIONS AT PRESENT RATES
INTERSTATE AND INTRASTATE
TEST YEAR 2003

	Sierrra			TD		
	Subject To Separations	Interstate	Intrastate[16] Total	Subject To Separations	Interstate	Intrastate[17] Total
	(a)	(b)	(c)= (a-b)	(d)	(e)	(f)= (d-e)
OPERATING REVENUES:						
1. Local Network Services	7,132,175		7,132,175	7,270,122		7,270,122
2 Local Servics - CHCF-A	13,955,628		13,955,628	10,898,442		10,898,442
3 Long Distance Network	18,049		18,049	0		
Network Access Svces:						
4 Intrastate	3,196,334		3,196,334	3,118,523		3,118,523
5 Interstate	11,495,520	11,495,520	0	11,563,085	11,563,085	0
6 Interstate - USF	5,160,814	5,160,814	0	5,803,376	5,803,376	0
7 Miscellaneous	1,507,637	0	1,507,637	1,617,858	0	1,617,858
8 LESS: Uncollectible Rev.	(11,126)		(11,126)	(11,341)		(11,341)
9 **Total Oper. Revenues**	**42,455,031**	**16,656,334**	**25,798,697**	**40,260,065**	**17,366,461**	**22,893,604**
OPERATING EXPENSES:						
10 Plant Specific	9,039,700	2,332,935	6,706,765	6,168,340	1,591,904	4,576,436
11 Plant Non-Specific (less depr.)	2,315,200	649,539	1,665,661	2,250,170	631,295	1,618,875
12 Depreciation & Amortization	10,529,077	2,683,543	7,845,534	10,434,911	2,659,543	7,775,368
13 Customer Operations	4,379,932	907,590	3,472,342	4,328,300	896,891	3,431,409
14 Corporate Operations	7,244,300	1,723,117	5,521,183	7,407,800	1,762,007	5,645,793
15 Interstate Expense Adj. -USF	0	5,160,814	(5,160,814)	0	5,803,376	(5,803,376)
16 **Total Oper. Expenses**	**33,508,209**	**13,457,538**	**20,050,671**	**30,589,521**	**13,345,016**	**17,244,505**
OPERATING TAXES:						
17 Operating State Inc. Taxes	689,654	256,522	433,132	752,888	329,054	423,834
18 Operating Fed Income Taxes	2,353,715	882,646	1,471,069	2,575,424	1,136,955	1,438,469
19 Taxes Other Than Income	655,500	167,650	487,850	663,900	169,798	494,102
20 **Total Operating Taxes**	**3,698,869**	**1,306,818**	**2,392,051**	**3,992,212**	**1,635,807**	**2,356,405**
21 **Net Operating Revenue**	**5,247,953**	**1,891,978**	**3,355,975**	**5,678,332**	**2,385,638**	**3,292,694**
RATE BASE (Beginning + End of Year Average)						
22 Telephone Plant-in-Service	128,072,519	33,374,850	94,697,669	126,452,595	32,952,709	93,499,886
23 Tel. Plt Under Construction	2,100,000	547,246	1,552,754	1,575,000	410,435	1,164,565
24 Mat & Supplies	750,000	203,661	546,339	750,000	203,661	546,339
25 Working Cash	1,533,208	270,008	1,263,200	1,426,908	270,008	1,156,900
26 Less: Deprec. Res.	(74,336,891)	(19,177,905)	(55,158,986)	(72,880,301)	(18,802,125)	(54,078,176)
27 Def. Taxes	(6,571,560)	(1,736,582)	(4,834,978)	(6,577,057)	(1,738,035)	(4,839,022)
28 Customer Deposit	(20,000)	(5,212)	(14,788)	(9,974)	(2,599)	(7,375)
29 RTB Stock	124,029	124,029	0	124,029	124,029	0
30 **Total Rate Base**	**51,651,305**	**13,600,095**	**38,051,210**	**50,861,200**	**13,418,083**	**37,443,117**
31 **Rate of Return**	**10.16%**	**13.91%**	**8.82%**	**11.16%**	**17.78%**	**8.79%**

[16] As original filed in December 2001, without company updates.
[17] Includes Sierra updates.

APPENDIX C
THE SIERRA TELEPHONE COMPANY, INC.
INTRASTATE RESULTS OF OPERATIONS
AT ADOPTED RATE OF RETURN
TEST YEAR 2003

		SIERRA[18] Proposed (a)	TD[19] Proposed (b)	UTILITY EXCEED STAFF AMOUNT (c)	Percent (d)	ADOPTED (e)
OPERATING REVENUES:						
1	Local Network Services	7,132,175	7,270,122	(137,947)	(1.9)	7,270,122
2	Local Services - CHCF-A	14,703,309	11,649,067	3,054,242	26.2	11,649,067
3	Long Distance Network	18,049	0	18,049	100.0	0
	Network Access Svces:					
4	Intrastate	3,196,334	3,118,523	77,811	2.5	3,118,523
5	Interstate	0	0	0	0.0	0
6	Interstate - USF	0	0	0	0.0	0
7	Miscellaneous	1,507,637	1,617,858	(110,221)	(6.8)	1,617,858
8	LESS: Uncollectible Rev.	(11,126)	(11,341)	215	(1.9)	(11,341)
9	**Total Oper. Revenues**	**26,546,378**	**23,644,229**	**2,902,149**	**12.3**	**23,644,229**
OPERATING EXPENSES:						
10	Plant Specific	6,706,765	4,576,436	2,130,329	46.5	4,576,436
11	Plant NSpecific (less depr.)	1,665,661	1,618,875	46,786	2.9	1,618,875
12	Depreciation & Amortization	7,845,534	7,775,368	70,166	0.9	7,775,368
13	Customer Operations	3,472,342	3,431,409	40,933	1.2	3,431,409
14	Corporate Operations	5,521,183	5,645,793	(124,610)	(2.2)	5,645,793
15	Interstate Expense Adj. -USF	(5,160,814)	(5,803,376)	642,562	(11.1)	(5,803,376)
16	**Total Oper. Expenses**	**20,050,671**	**17,244,505**	**2,806,166**	**16.3**	**17,244,505**
OPERATING TAXES:						
17	Operating State Inc. Taxes	499,227	490,189	9,038	1.8	490,189
18	Operating Fed Income Taxes	1,702,809	1,671,123	31,686	1.9	1,671,123
19	Taxes Other Than Income	487,850	494,102	(6,252)	(1.3)	494,102
20	**Total Operating Taxes**	**2,689,886**	**2,655,414**	**34,472**	**1.3**	**2,655,414**
21	**Net Operating Revenue**	**3,805,821**	**3,744,310**	**61,511**	**1.6**	**3,744,310**
RATE BASE (Beginning + End of Year Average)						
22	Telephone Plant-in-Service	94,697,669	93,499,886	1,197,783	1.3	93,499,886
23	Tel. Plt Under Construction	1,552,754	1,164,565	388,189	100.0	1,164,565
24	Mat & Supplies	546,339	546,339	0	0.0	546,339
25	Working Cash	1,263,200	1,156,900	106,300	9.2	1,156,900
26	Less: Deprec. Res.	(55,158,986)	(54,078,176)	(1,080,810)	2.0	(54,078,176)
27	Def. Taxes	(4,834,978)	(4,839,022)	4,044	(0.1)	(4,839,022)
28	Customer Deposit	(14,788)	(7,375)	(7,413)	100.5	(7,375)
29	RTB Stock	0	0	0	0.0	0
30	**Total Rate Base**	**38,051,210**	**37,443,117**	**608,093**	**1.6**	**37,443,117**
31	**Rate of Return**	**10.00%**	**10.00%**			**10.00%**

[18] As Original filed in December 2001, without company updates.
[19] Includes Sierra updates.

APPENDIX D

THE SIERRA TELEPHONE COMPANY, INC.
ADOPTED NET-TO-GROSS MULTIPLIER
INTRASTATE REVENUE REQUIRMENT AND CHCF-A SUPPORT
TEST YEAR 2003

1	Gross Revenues		1.00000
2	Uncollectibles[20]		0.00000
3	Net Revenues		1.00000
4	State Income Tax (Tax Rate times ln 3.)	8.84%	0.08840
5	Federal Taxable Income (ln 3. less ln 4.)		0.91160
6	Federal Income Tax (Tax Rate time ln 5.)	34.00%	0.30994
7	Net Income (ln 5. less ln 6.)		0.60166
8	**NET TO GROSS MULTIPLIER** (ln 1. divided by ln 7.)		**1.66207**
	Intrastate Revene Requirement		
9	Adopted State Rate Base		$37,443,117
10	Net Revenues Adopted at 10.00%	10.00%	$3,744,312
11	Net Revenues at Present Rates		$3,292,691
12	Change in Net Revenues (ln 10. less ln 11.)		$451,621
13	**GROSS REVENUE CHANGE REQUIRED (ln 12. times ln 8.)**		**$750,626**
	CHCF-A Support		
14	Recovery of Rate Case Expenses (3-year amortization)		$0
15	2003 CHCF-A Support at Present Rates		$10,898,442
16	2003 CHCF-A Support Adopted (ln 15. add ln 13.)		**$11,649,068**

[20] Uncollectibles are included in Line 1, Gross Revenues.